No. 10204.

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

CLAUDE R. FOOSHE,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITIONER'S OPENING BRIEF.

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Jurisdiction.

Petitioner filed his income tax return for the calendar year 1938 in Los Angeles, California. An asserted deficiency in income for that year in the amount of $1,436.47 was determined by the Commissioner of Internal Revenue. The Board of Tax Appeals affirmed the determination of the Commissioner. This case is before this Honorable Court on petition to review a decision of the United States Board of Tax Appeals under Section 1142 of Title 26, United States Code. The decision of the United States Board of Tax Appeals was entered January 28th. 1942. The petition was filed April 23rd, 1942.

Question Presented.

Whether certain sums of money received by petitioner during the period May 1st, 1938, to December 31st, 1938, from Prudential Insurance Company were community income to petitioner and his wife, Lura D. Fooshe, or separate income to petitioner.

Statement.

The facts were stipulated. [Tr. pp. 14-53.]

Petitioner and his wife, Lura D. Fooshe, were residents of and domiciled in the State of California from May 1st, 1938, to December 31st, 1938. [Stip. No. 19, Tr. p. 53.] They filed separate returns for the year 1938 with the Collector of Internal Revenue in Los Angeles. [Stip. No. 20, Tr. p. 53.]

During this period from May 1st, 1938 to December 31st, 1938, petitioner received certain sums of money totaling $21,504.80 from the Prudential Insurance Company of America (hereinafter referred to as the "Company"), which were reported by petitioner and his wife on their separate income tax returns as community income. [Stip. No. 20, Tr. p. 53.] The respondent has included the entire amount in the taxable income of the petitioner. [Stip. No. 9, Tr. pp. 16-17.]

Prior to May 1st, 1938, petitioner and his wife had lived in St. Louis, Missouri, where petitioner was manager of an Ordinary Agency of the Company. Petitioner had operated the St. Louis Agency of the Company under

a contract of employment dated August 4th, 1919* [Exhibit B, Tr. pp. 36-39], as amended by an agreement dated May 17th, 1927.* [Exhibit C, Tr. p. 40; Stip. No. 8, Tr. p. 16.] This contract as amended will be referred to as the St. Louis Agency contract. This contract provided, among other things, that petitioner was to act as manager of a certain designated territory in Missouri for the purpose of procuring applications for insurance, for the further purpose of collecting and paying over premiums to the Company, and performing such other managerial duties as the Company might require. [Sec. 1, p. 27, Ex. 1 hereof.] During the continuance of the contract, and only upon the express condition that the manager as such remain continuously in the employ of the Company, the manager received as compensation a commission on premiums based upon a schedule set forth in the contract. [Sec. 3, p. 28, Ex. 1 hereof.] This schedule provided for certain percentages of premiums paid in the first policy year and of renewal premiums paid in succeeding years. The commissions based on premiums in the first policy year are not involved here, and it was stipulated that under the contract the petitioner as manager was entitled to receive only 2½% of renewal premiums, the balance of the percentages provided for in the schedule in Section 3 being paid to agents working under the manager. [Stip. 9, Tr. pp. 16-17, and

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*The contract of August 4th, 1919 [Exhibit B, Tr. pp. 36-39] and the amendment of May 17th, 1927 [Exhibit C, Tr. p. 40] are set forth as Exhibits 1 and 2 hereof, respectively, inasmuch as the photostatic copies of the contracts in the transcript are difficult to read.

Stip. 15, p. 19.] For the collection of premiums of all policies for which no provision for compensation to the manager was made under the schedule of Section 3, the manager received a collection fee of 2% of the premiums, and on the other hand, if the premium of any policy covered by the contract was not collected by the manager, the Company charged a collection fee of 2% of the premium. This collection fee was deducted from the commission otherwise payable under the contract. [Sec. 4, p. 30, Ex. 1 hereof.]

Upon termination of the contract, the manager was allowed the commission upon renewal premiums, less the Company's collection fee of 2% of the premium. The number of years for which the manager would receive these commissions was dependent upon the cause of the termination and the length of service of the manager. [Sec. 6, p. 31, Ex. 1 hereof.] Thus, petitioner, upon termination of the contract, after deduction of the Company's collection fee of 2% of the premium, would be entitled to receive ½% of the renewal premium. [Stip. 14, Tr. pp. 18-19.] The contract also provided that upon its termination the compensation paid to the manager should be in full settlement of all claims under the contract and that all compensation which a continuance of the contract might have secured to him shall cease except as provided in the contract. [Sec. 21, p. 36, Ex. 1 hereof.]

The amendments effected by the agreement of May 17th, 1927, related to collection fees and terminal commissions. Certain modifications in the collection fee allowed the manager on group insurance and in certain other instances were made. Certain allowances were also made in connection with terminal commissions in some cases, not here material. Section B, which provided that

the Company would pay commissions on renewal premiums up to and including the tenth policy year, less a collection fee of 2% of the premium, was substantially a restatement of the first paragraph of Section 6 of the original agreement.

Petitioner continued to serve as manager of the St. Louis Agency until April 30th, 1938. On May 2nd, 1938, petitioner became manager of an Ordinary Agency of the Company in Los Angeles, California. Prior to the date on which petitioner became manager of the Los Angeles Agency, the St. Louis Agency contract was terminated. [Ex. F, Tr. p. 49.] The Company proposed that the petitioner operate the Los Angeles Agency under what was called "New Terms" manager's contract, which provided for a guaranteed monthly salary and certain commissions on first year premiums instead of the compensation derived from commissions and collection fees provided for in the St. Louis Agency contract.

The business in force in the St. Louis Agency was approximately 49 million dollars at the close of business December 31st, 1937, and over 5 million dollars of new insurance had been written in the St. Louis Agency under petitioner's supervision during the year 1937. [Stip. No. 10, Tr. p. 17.] At the close of business December 31st, 1937, there was in effect in the Los Angeles Agency approximately 29 million dollars of insurance, and approximately $800,000 in new insurance had been written in the Los Angeles Agency during the year 1937. [Stip. No. 11, Tr. p. 17.] With this volume of business in the Los Angeles Agency, petitioner would have suffered a substantial reduction in compensation in taking over the Los Angeles Agency under his New Terms contract with the proposed salary of $600 a month. [Stip. No. 12, Tr. pp.

17-18; Statement of George H. Chace, Tr. p. 52.] In order that petitioner should not suffer the deduction in compensation which would result from the New Terms contract as applied to the Los Angeles Agency, the Company agreed to relinquish its collection fee of 2% of the renewal premiums to which it was entitled upon the termination of the St. Louis Agency contract. Thus, instead of receiving ½% of the renewal premiums as provided upon the termination of the St. Louis Agency contract, petitioner would receive 2½% of the amount of the renewal premiums. [Stip. No. 14, Tr. pp. 18-19.] It was agreed that this would provide petitioner with ample compensation for the supervision of the Los Angeles Agency. [George H. Chace Statement, Ex. 14, Tr. pp. 51-52.] The petitioner and the Company exchanged letters confirming this arrangement. [Ex. D, Tr. pp. 41-44, and Ex. E. Tr. pp. 44-47.]

It should be stated here that the petitioner has conceded throughout the proceeding that the ½% of the renewal premiums which petitioner was entitled to receive in any event upon the termination of the St. Louis Agency contract, was separate income to him, and that the part of the $21,504.80 received by petitioner in California which this ½% represents was properly included by respondent in petitioner's taxable income. It is the part of the $21,504.80 represented by the relinquishment of the 2% collection fee which is in issue here. Petitioner's position is that these sums represent part of his compensation as manager of the Los Angeles Agency, and as such are community income.

Specifications of Error to Be Urged.

The Board of Tax Appeals erred:

1. In finding, holding and deciding that the major portion of the sum of $21,504.80 was the separate income of petitioner under the laws of the State of California.

2. In not finding, holding, and deciding that said income was the income of the community composed of petitioner and his wife, Lura D. Fooshe, under the laws of the State of California.

3. The Board of Tax Appeals erred in construing the evidence as determining that said income was the separate income of the petitioner.

4. The Board of Tax Appeals erred in that the conclusion of law arrived at, namely, that the income was the separate income of petitioner, is not supported by and is contrary to the findings of fact.

Summary of Argument.

In demonstrating that the sums of money received by petitioner during the period from May 1st, 1938, through December 31st, 1938, by reason of the relinquishment by the Prudential Insurance Company of its 2% collection fee on certain renewal premiums collected in the St. Louis Agency were community income, petitioner will develop three propositions:

A. Upon termination of the St. Louis Agency contract, by its express terms and under settled principles of law, petitioner did not have any claim or right of any

kind to the collection fee on renewal premiums. The collection fee was the agreed measure of compensation for services rendered in collecting the premiums under the contract and was received by the party performing the collection service. Upon termination of the contract petitioner had no further right to perform the service or receive the collection fee. Services rendered in writing the policy of insurance were compensated for by the payment of the ½% commission which was received by petitioner irrespective of the collection fee.

B. Sums received by petitioner by reason of the relinquishment of the Company's 2% collection fee represented part of the compensation for petitioner's services as manager of the Los Angeles Agency. These sums were received under the agreement entered into between the Company and petitioner for his employment as manager of the Los Angeles Agency.

C. That the character of income as community or separate under the laws of California is to be determined in accordance with the laws of the husband's domicile at the time the income is earned. Income is earned under this rule of law at the time the services for which the income is received, are performed. Thus inasmuch as the services were rendered in California at a time when petitioner was domiciled here, under this settled rule of law, the sums received by petitioner as a result of the relinquishment of the Company's 2% collection fee were community income.

ARGUMENT.

I.

Upon Termination of the St. Louis Agency Contract, by Its Express Terms and Under Settled Principles of Law, Petitioner Did Not Have Any Claim or Right of Any Kind to the Collection Fee on Renewal Premiums.

While petitioner was manager of the St. Louis Agency, his rights to compensation for the services he performed were determined by the contract of August 4th, 1919, as amended May 17th, 1927, referred to herein as the St. Louis Agency contract. [Exhibits 1 and 2 hereof.] Under this contract, his employment was to act as manager.

> "for the purpose of procuring applications for Ordinary Insurance in the said Company, with premiums payable annually, semi-annually, or quarterly, and *for the further purpose of collecting and paying over premiums to the company in cash on such insurance when effected*, and of performing such other duties in connection therewith as may be required by said company;" [Sec. 1, p. 27, Ex. 1 hereof.] (Italics ours.)

Petitioner's duty as manager to collect and pay over premiums is here emphasized inasmuch as it clearly appears from other provisions of the contract that the portion of his compensation represented by the company's 2% collection fee here in question, when received by him under the contract, was compensation for services he performed in collecting and paying over the premiums. Thus, Section 4 provides that after the expiration of the period for which provision for commissions is made in Section 3

(15 years as to regular policies and 6 years as to intermediate policies)

> "the manager shall be entitled to a collection fee of 2% of such premiums, but the payment of such collection fees shall be subject to discontinuance at any time in the event of the Company making other arrangements for the collection of the premiums, and, if not previously discontinued, shall cease upon the termination of this contract."

The allowance of the 2% collection fee to the manager in such cases is clearly compensation for the services performed in making the collection. Paragraph 2 of Section 4 provides:

> "Provided, however, that when premiums, either first or renewal, on policies issued under this contract are collected *other than by the manager* during the continuance of this contract, a collection fee of 2% of such premiums shall be deducted from the commission to be allowed as provided in Section 3." (Italics ours.)

This paragraph, providing as it does, that if the premium on any policy is not collected by the manager, a collection fee of 2% of the premiums shall be deducted from the amount received by the manager, clearly indicates that the 2% of the premium received by the manager when the premium is collected by him represents compensation for his services of collection.

Paragraph 3 of Section 4 provides:

> "Provided, further, that on premiums on business not issued by or through the Manager but transferred to him for collection, he shall be allowed a collection fee of 2% of the premiums, which collec-

> tion fees, however, may be discontinued at any time in the event of the Company making other arrangements for the collection of the premiums."

With this provision the possibilities that might arise in connection with the collection of premiums are completely covered and it demonstrates beyond any doubt that the 2% collection fee represents compensation for the collection of the premiums. The right to receive the 2% collection fee clearly arises from the performance of the duties involved in collection of premiums and does not arise from the writing of the policy. The petitioner did not have any right or claim of any kind to the collection fee by reason of the policy of insurance having been written in his agency inasmuch as the collection fee was earned each year in which it was paid through the performance of the collection services.

Thus, if the St. Louis Agency contract had not been terminated and the petitioner had transferred to the Los Angeles Agency, he would not have received the 2% collection fee on premiums of policies of insurance written while he was manager of the St. Louis Agency. He would only have been entitled to a collection fee of 2% on the premiums being collected in the Los Angeles Agency.

Inasmuch as the petitioner as manager was entitled under the St. Louis Agency contract to receive only 2½% of the renewal premiums collected (the balance of the percentage set forth in Section 3 being paid to the agent [Stip. No. 15, Tr. p. 19]), the petitioner as manager would only have had the right to receive ½% of the renewal commission if the renewal premium was not collected under his supervision. [Sec. 4, p. 30, Ex. 1, hereof.] [Stip. No. 14, Tr. pp. 18-19.]

The St. Louis Agency contract, however, was terminated, effective on April 30th, 1938. [Ex. F, Tr. p. 49.] Originally petitioner's rights upon termination of the contract of August 4th, 1919 were determined by Section 6. [Sec. 6, Ex. 1 hereof.]

Section 6 was amended by the provisions of the agreement of May 17th, 1927 relating to terminal commissions. [Ex. 2 hereof.] Inasmuch as the contract was not terminated under the conditions of Paragraphs a or c of the provisions relating to terminal commissions in this agreement, the rights of the petitioner are to be determined by Paragraph b. The right to commissions based on the premiums of policies written in the St. Louis Agency under his supervision was absolutely dependent upon this provision. He did not have any inherent right or claim, either legal or equitable, in or to commissions or collection fees on renewal premiums except as therein provided.

Wagner v. Land, 152 Okla. 225, 4 Pac. (2d) 81;

Fabian v. Provident Life & Acc. Ins. Co., 5 Fed. Supp. 806;

Locher v. New York Life Ins. Co., 200 Mo. App. 659, 208 S. W. 862;

Arensmeyer v. Metropolitan Life Ins. Co., 254 Mo. 363, 162 S. W. 261;

Nelles v. MacFarland, 9 C. A. 534, 99 Pac. 980;

Walker v. John Hancock Life Ins. Co., 80 N. J. L. 342, 79 Atl. 354;

79 *A. L. R.* 475;

136 *A. L. R.* 160.

In *Wagner v. Land, supra*, a sub-agency contract between Land, a manager of the Prudential Insurance

Company, and an agent, Wagner, was before the court. While the provisions of that contract were identical in many respects with the St. Louis Agency contract, the right of the sub-agent to receive commissions after the termination of the contract was limited to first year commissions less the collection fee of 2%. Wagner, the agent, sued the manager for renewal commissions after the termination of the agency. The court held that the agent had no right to such commissions. The court stated that under that contract the right to renewal commissions was dependent upon the continuance of the contract. The court emphasized the provisions of the contract which is to be found as Section 21 in the St. Louis Agency contract. [Ex. 1 hereof.] This section provides that the compensation paid to the manager shall be in full settlement of all claims and demands in favor of the management under the contract and that he shall have no other rights to compensation which a continuance of the contract might have secured to him.

Nelles v. MacFarland, supra, also involves a contract between a manager of Prudential Insurance Company and a sub-agent.

Locher v. New York Life Insurance Co., supra, is one of the leading cases and states the rule as follows (208 S. W. 862, 866):

> "The right of the agent to commissions on renewals collected or falling in after the end of his agency can rest only on express terms in his contract, or be necessarily drawn from an interpretation of that contract as a whole. This must be so for the right to commissions on renewals rests, in part, on the consideration of the services by the agent to the company in keeping the policies written by him alive."

In the St. Louis Agency contract, the parties had placed a definite value on the services of the manager for collecting the premiums and keeping the policies in force. This was the 2% collection fee.

The lack of any right of the agent to the collection fee or renewal commissions is very neatly raised in *Walker v. John Hancock Life Insurance Co., supra.* In that case, under his contract the agent received an amount equal to nine times the first premium for writing the policy and a 20% commission for collecting the premiums. The contract was cancelled by the company and the agent sued for damages suffered as a result of his being deprived of his "right" to continue to make collections and receive his 20% commission. The court held that he had no right to continue to collect the premium from the fact of the writing of the policy or otherwise than as provided in his contract. Judgment for the company was affirmed.

Thus, the petitioner had no right or claim in or to the portion of the renewal commissions represented by the 2% collection fee, nor did the portion of the renewal commission represented by the collection fee reflect work or services which petitioner had performed in any way. The collection fee was not earned and the services for which it was compensation were not rendered until the collection of the premium was made by the manager.

> The Board of Tax Appeals was of the opinion that "the 2½% to which, before deduction of collection fee by the company, the petitioner was entitled, was based upon services rendered at St. Louis." [Tr. p. 67.]

The error of this statement is obvious. The petitioner was not entitled to 2½% without deduction of the 2%

collection fee unless he performed the services in St. Louis of collecting the premiums. Upon termination of the contract, petitioner had no right whatever to the amount represented by the collection fee, first, because his contract expressly so provided, and secondly because he could not perform the service of collecting the premium for which the collection fee was compensation. Petitioner's only right, based upon services rendered in St. Louis, was to the ½% which was payable to petitioner after the termination of the contract, and was not dependent upon the rendering of the service of collecting the premium. This ½% was based upon services rendered in St. Louis in writing the policy and under the contract it was the full measure of his compensation for such service. The error contained in the statement made by the Board of Tax Appeals is the error of its decision.

II.

Sums Received by Petitioner by Reason of the Relinquishment of the Company's 2% Collection Fee Represented Part of the Compensation Earned by Petitioner in California.

In the early part of 1938 negotiations were commenced between petitioner and the Company with reference to petitioner's taking over the Los Angeles Agency. The question of compensation was paramount inasmuch as the St. Louis Agency was at that time a larger agency than the one in Los Angeles. The insurance in force in the St. Louis Agency was approximately 49 million dollars, and in the prior year new business in an amount exceeding 5 million dollars had been written. [Stip. No. 10, Tr. p. 17.] Insurance in force in the Los Angeles

Agency amounted to approximately 29 million dollars, and approximately $800,000 of new business had been written in the prior year. [Stip. No. 11, Tr. p. 17.] It also appeared that the Company had changed its managerial contracts to what is referred to as a "new terms" contract.

The manager's contract [Ex. A, Tr. pp. 20-35], is a "new terms" contract. It provides for a minimum guaranteed salary and certain commissions on first year premiums. No collection fees and no commissions on renewal premiums are allowed, as was the case in the St. Louis Agency contract. The taking of the Los Angeles Agency under this "new terms" contract would have resulted in a substantial decrease in petitioner's compensation. [Stip. No. 12, Tr. p. 18.]

The considerations affecting the action of the parties in the negotiations and the agreement which resulted are set forth in the statement of Mr. Chace, Vice-President of the ordinary agencies of the Company. He indicates that Mr. Fooshe would have suffered a substantial reduction in income by taking the Los Angeles Agency under the "new terms" contract with the guaranteed salary of $600 a month then tentatively proposed. The Company, however, did not feel that it could undertake to guarantee the substantially larger salary that would have been required to make Mr. Fooshe's compensation in the Los Angeles Agency under the "new terms" contract equal that which he received under the St. Louis

Agency contract. In this situation, it was agreed that petitioner should receive a guaranteed salary of $600 a month and receive additional sums measured by the amount which relinquishment by the Company of its 2% collection fee on renewal premiums payable on business issued through the St. Louis Agency would represent.

This arrangement was satisfactory inasmuch as petitioner would receive an amount comparable to that which he received in the St. Louis Agency at the time he took over the Los Angeles Agency. The compensation derived from the collection fee would diminish as it was computed upon renewal premiums received through the tenth year of the life of the policy. Manifestly, the intention of the parties was that the sums measured by the Company's 2% collection fee would constitute compensation for services performed in the Los Angeles Agency in addition to the salary and the amount in first year commissions the volume of business in that agency would produce until petitioner had developed the agency to a point where his earnings under the "new terms" contract would equal his earnings under the St. Louis Agency contract.

Mr. Chace expressed this intention thus:

> "It was felt by waiving this 2% collection fee that the amount that would accrue to Mr. Fooshe, together with the guaranteed salary to be paid him, would be ample compensation for the supervision of the Los Angeles Agency." [Ex. H, Tr. p. 52.]

On February 23rd, 1938, petitioner sent a letter to Mr. Chace, expressing this agreement. [Ex. D, Tr. pp.

41-44.] Petitioner's expression of his understanding of the agreement is contained in the postscript [Tr. pp. 43-44]:

> "I understood I would receive the full renewals same as had I remained here, only the company will bear the expense for collecting to the tenth year. I presume all of this is set out in a letter so will leave it all to you."

To which Mr. Chace replied under date of February 24th, 1938 [Ex. E, Tr. pp. 44-47]:

> "Referring to your postscript, you are correct in your understanding that full renewals will be paid on the business in the St. Louis Agency after the termination of the 'Old Terms' contract, just as though the contract remained in force. In other words, no collection fee will be imposed on the business for which you have qualified for renewal commissions. Naturally, the collection fee that you would receive if you remained in St. Louis under the Old Terms contract on business on which your renewal business has expired, would be discontinued."

In other words, petitioner was to receive the 1/2% to which he was entitled in any event upon the termination of the contract, and in addition thereto, the 2% represented by the Company's collection fee. The Company was, in effect, engaging services to be rendered in Los Angeles in managing the Los Angeles Agency, in lieu of services to be rendered in collecting the renewal premiums in the St. Louis Agency.

III.

The Character of Income as Community or Separate Under the Laws of California Is to Be Determined in Accordance With the Laws of the Husband's Domicile at the Time the Income Is Earned.

Fundamentally, there is no dispute as to the facts in this proceeding. The error arises in the application of legal principles to the facts which were stipulated and incorporated by the Board of Tax Appeals in its Findings of Fact.

The first error was as has already been stated, in concluding that the petitioner had any right or claim, legal or equitable, in or to the 2% collection fee upon the termination of the contract in the face of the well-established rule of law to the contrary. The second error is as to the law of community property and income.

That the character of income as community or separate under the laws of California is to be determined in accordance with the laws of the husband's domicile at the time the income is earned is well settled.

U. S. v. Malcolm, 282 U. S. 792;

Commissioner v. Cavanaugh, 125 Fed. (2d) 336, (C. C. A. 9);

Devlin v. Commissioner, 82 Fed. (2d) 731, (C. C. A. 9);

W. L. Honnold, 36 B. T. A. 1190;

Sarah R. Preston, 35 B. T. A. 312;

Gouverneur Morris, 31 B. T. A. 178;

California Civil Code, Sec. 161 A;

California Civil Code, Sec. 162;

California Civil Code, Sec. 163;

California Civil Code, Sec. 164.

These cases likewise clearly establish the rule of law that income is earned at the time the service or work for which income is received is performed.

In its opinion [Tr. pp. 66-69], the Board of Tax Appeals cites the cases of *Sarah R. Preston, supra; John M. King,* 26 B. T. A. 1128 (Aff. 69 Fed. (2d) 639); *William Semar,* 27 B. T. A. 494; *W. L. Honnold, supra,* and *Albert J. Houston,* 31 B. T. A. 188, as establishing the doctrine of inchoate rights with reference to community income property. The doctrine of inchoate rights is well established. The Board of Tax Appeals failed to perceive, however, that the very cases it cited established two corollary propositions which require a conclusion contrary to that reached by the Board.

The first corollary is that the inchoate right must be legal or equitable in character. The second corollary is that performance of the services for which the income is received is that which gives rise to the right, inchoate or otherwise, to the income.

Thus, in *Sarah R. Preston, supra,* which involved the determination of the community or separate character of legal fees received after the date on which the wife acquired a vested interest in community income in California, the Board of Tax Appeals expressly pointed out (p. 323):

> "Preston performed services for which he received a part of the Herminghaus fee prior to July 29,

> 1927, the effective date of section 161 (a) of the Civil Code of California. *He performed no services under the contract after that date.* Since Preston would have been taxable upon the fees if they had been received prior to the effective date, he is likewise taxable upon those received after that date; for the amendment to the Civil Code did not serve to change separate property into community property." (Italics ours.)

Similarly, as to the quotation from McKay on *Community Property,* Section 517, (set forth in the *Preston* case and requoted by the Board in its opinion in the instant case [Tr. p. 68]), in which the doctrine of inchoate rights is expressed, reference to McKay's complete statement of the doctrine in Section 517 discloses the premise upon which the quoted passage is based:

> "The reader should notice that it is assumed the initial right of the series is of such a character that it is recognized as valid in law or equity and is available against some one. It must be more than a mere unenforceable claim." (*McKay, Community Property,* Second Edition, p. 352.)

As it has been demonstrated, petitioner had no right or claim of a legal or equitable nature in or to the 2% collection fee upon the termination of the St. Louis Agency contract. Therefore, his right to the sums received by reason of the relinquishment of the 2% collection fee by the Company could not have their inception in the St. Louis Agency contract, as the Board of Tax Appeals states, under any proper application of the doctrine of inchoate rights. The services which gave rise to the right to receive the sums measured by the 2% collec-

tion fee were those performed in California as manager, and the contract in which this right had its inception was petitioner's agreement of employment for the Los Angeles Agency. These services were not the "condition" of the receipt of the moneys. They were the *sine qua non,* that gave rise to his right to the money.

If the statements of the Board of Tax Appeals are correct and the rendering of services under a contract of employment is only "compliance with a condition" the precedent of all prior cases is swept away and there is a new community property law under which the character of income as separate or community is to be determined by the law of the state where the contract was entered into and not by the laws of the state of the domicile of the husband at the time the services are performed. Community property states would become the situs for the making of all contracts and the present trend in tax collections would be reversed. Conversely the community interest of a wife could be fraudulently defeated by the making of a contract in a noncommunity property state. This cannot be and is not the law. The error is obvious. The performance of services is that which gives substance to the right to income and the character of the income as community or separate is fixed at the time the services are rendered.

Similarly in *William Semar, supra,* the services which gave rise to Semar's right in the corporation had all been performed and completed prior to his marriage, although he had not completed his acquisition of the interest in the corporation to which his services gave him a right. It was therefore held that his interest in the company was his separate property.

And in the *Honnold* case, *supra*, the services had all been performed in New York while petitioner was a resident of that state. It was expressly stated in the opinion that petitioner was not rendering and had not rendered any services to the company while domiciled in California in which would form any basis for the right to the corporate disbursement he received.

Likewise in the *Houston* case, *supra*, the petitioner's services had all been performed prior to his marriage, although the money was received after this event. It was therefore held that the moneys received were his separate property.

In the *John M. King* case, *supra*, involving the community or separate character of an attorney's contingent fee which was received after the death of the taxpayer's wife, the Circuit Court of Appeals held that the contingent fee was community income. It appeared that while the greater part of the services had been rendered under the contingent contract prior to the death of the taxpayer's wife, some services had been rendered after her death. The court treated the contingent fee contract as an entirety in determining that it was community in character. It was expressly noted by the court, however, that the parties had not raised the question as to whether a deduction should not have been made from the community income of the taxpayer's wife because of the services and expenses of the taxpayer after her death. Thus, while the contract before the court was truly dependent upon a condition: *i. e.*, successful outcome of litigation, the court expressly limited its decision by noting that the services under such a contract, although the contract itself must be treated as an entirety, might give rise to distinct community or separate interest.

In the instant case, petitioner, having no rights whatever in the 2% collection fee upon the termination of the St. Louis Agency contract, entered into a contract which gave him a right to receive the sums of money measured by the 2% collection fee by performing services of manager in the Los Angeles Agency.

Further examination of the cases cited, *supra,* would only be to belabor the rule of law uniformly applied in determining the character of income derived from the rendering of services, namely, that the character of the income is determined at the time the services are performed. The services having been performed in California at a time when petitioner was domiciled in California, the income derived therefrom must be community income.

Conclusion.

It clearly appearing that the petitioner had no claim or right, either legal or equitable, in or to that part of the $21,504.80 represented by the moneys derived by the Company from its 2% collection fee upon the termination of the St. Louis Agency contract; it further appearing that such moneys were paid to petitioner for managerial services performed in the Los Angeles Agency under a contract of employment calling for such services, the conclusion under well settled principles of law is inescapable that such sums were earned by petitioner at a time when he was domiciled in California and consequently constituted income to the community of petitioner and his wife, Lura D. Fooshe, under California law.

As to that portion of the $21,504.80 represented by moneys derived by the Company from its 2% collection fee and paid to petitioner during the period from May 1st, 1938 until December 31st, 1938, the determination of the Commissioner of Internal Revenue was erroneous and the decision of the Board of Tax Appeals affirming the Commissioner's determination was likewise founded in error.

It is therefore respectfully submitted that an order be entered setting aside the decision of the Board of Tax Appeals and requiring the Commissioner to make a re-determination in accordance with the law. Inasmuch as petitioner has already paid the full amount of the deficiency assessed by the Commissioner during the course of this proceeding, the further order of this court is requested requiring repayment of such part of the payment as may be due petitioner under the rule of law in this case, together with interest thereon.

Respectfully submitted,

JOHN L. WHEELER,

Attorney for Petitioner.

APPENDIX.

THIS CONTRACT, made this Fourth day of August, 1919, by and between THE PRUDENTIAL INSURANCE COMPANY OF AMERICA, of Newark, N. J., party of the first part, and CLAUDE R. FOOSHE, of ST. LOUIS, in the County of ST. LOUIS and State of MISSOURI, party of the second part.

WITNESSETH: That the said parties, in consideration of the sum of one dollar each to the other in hand paid, and of the covenants and agreements hereinafter mentioned, hereby mutually covenant and agree, each with the other, as follows, to wit:

Section 1. That the said party of the first part, hereinafter designated as the Company, doth hereby appoint the said party of the second part, hereinafter designated as the Manager, as Manager for the following territory: Missouri east of and including counties of Putnam, Sullivan, Linn, Chariton, Howard, Boone, Moniteau, Morgan, Camden, Dallas, Webster, Douglas and Ozark, for the purpose of procuring applications for Ordinary Insurance in the said Company with premiums payable annually, semi-annually or quarterly, and for the further purpose of collecting and paying over premiums to the Company in cash on such insurance when effected, and of performing such other duties in connection therewith as may be required by said Company; and that this contract shall be treated as strictly confidential.

Section 2. That the Manager shall devote his entire time, talents and energies to the business of the Com-

pany and appoint agents in the territory named, for whose fidelity and honesty he shall be held responsible.

Section 3. That during the continuance of this contract and only upon the condition that the Manager, as such, remains continuously in the employ of the Company the compensation to be allowed the Manager shall be a commission on premiums when collected and paid to the Company in cash on policies written by or through him under this contract, as follows:

Regular Policies	Per Cent. of Premiums in the First Policy Year	Per Cent. of Premiums in the Second to the Tenth Policy Year, Inclusive	Per Cent. of Premiums in the Eleventh to the Fifteenth Policy Year, Inclusive
Whole Life	50	7½	5
30-Payment Life	45	7½	5
25-Payment Life	45	7½	5
20-Payment Life	40	7½	5
15-Payment Life	35	7½	5
10-Payment Life	30	7½	
5-Payment Life	15	7½	
30-Year Endowment	40	7½	5
25-Year Endowment	35	7½	5
20-Year Endowment	30	7½	5
15-Year Endowment	25	5	5
10-Year Endowment	20	5	
5-Year Endowment	10	5	
20-Payment 30-Year Endowment	35	7½	5
15-Payment 30-Year Endowment	35	5	5
15-Payment 25-Year Endowment	30	5	5
15-Payment 20-Year Endowment	25	5	5
10-Payment 25-Year Endowment	25	5	
10-Payment 20-Year Endowment	25	5	
10-Payment 15-Year Endowment	20	5	
20-Pay Pay't Life Pure End't Addition at end of 20 Years	40	7½	5
10-Year Term	30	7½	
Preliminary Term (Commission not allowed until regular premium is paid)	7½		
Single-Payment	5		
Annuity	2		
Extra Premiums	5		
One Year Renewable Term Group Insurance	10	5	

Intermediate Policies	Per Cent. of Premiums in the First Policy Year	Per Cent. of Premiums in the Second to the Sixth Policy Year, Inclusive
Whole Life	35	5
20-Payment Life	30	5
15-Payment Life	25	5
10-Payment Life	25	5
20-Year Endowment	30	5
15-Year Endowment	20	5
10-Year Endowment	15	5

Section 4. That on renewal premiums for the sixteenth and subsequent policy years, on Regular policies and for the seventh and subsequent policy years on Intermediate policies collected through his agency, on new business effected by or through the Manager under this contract, the Manager shall be entitled to a collection fee of two per cent (2%) of such premiums, but the payment of such collection fees shall be subject to discontinuance at any time in the event of the Company making other arrangements for the collection of the premiums, and, if not previously discontinued, shall cease upon the termination of this contract.

Provided, however, that when premiums, either first or renewal, on policies issued under this contract are collected otherwise than by the Manager during the continuance of this contract, a collection fee of two per cent (2%) of such premiums shall be deducted from the commission to be allowed as provided in Section 3.

Provided further, that on premiums on business not issued by or through the Manager, but transferred to him for collection, he shall be allowed a collection fee of two per cent (2%) of the premiums, which collection fees, however, may be discontinued at any time in the event of the Company making other arrangements for the collection of the premiums.

Section 5. That if this contract shall be terminated for any cause, except violation of its conditions, the commissions on the balance of the first year's premiums on policies issued through the Manager remaining unpaid at the termination of this contract, shall be payable to the Manager, his executors, administrators or assigns, subject to the conditions of Section twenty-three (23).

Section 6. That if this contract shall be terminated for any cause other than violation of its conditions, or the death of the Manager, and the Manager has been continuously in the service of the Company for two or more years, the Company will continue to pay to the Manager, his executors, administrators or assigns, the commissions upon renewal premiums on Regular policies as set forth in Section three (3) less a collection fee of two per cent (2%) of such renewal premiums, until the commissions on the premiums in the tenth year of insurance shall have been paid, subject to the conditions of Section twenty-three (23).

That if this contract shall be terminated by the death of the Manager and if he has been continuously in the service of the Company for two or more years, the Company will continue to pay to his executors, administrators or assigns, the commissions upon renewal premiums on Regular policies as set forth in Section three (3) less a collection fee of two per cent (2%) of such renewal premiums, until the commissions on the premiums in the fifteenth year of insurance shall have been paid, subject to the conditions of Section twenty-three (23).

That if this contract shall be terminated for any cause other than violation of its conditions before the Manager shall have been continuously in the service of the Company for two years, the Company will continue to pay to the Manager, his executors, administrators or assigns, the commissions upon renewal premiums as set forth in Section three (3) less a collection fee of two per cent (2%) of such renewal premiums, until the commissions on the premiums in the sixth year of insurance shall have been paid, subject to the conditions of Section twenty-three (23).

That if this contract shall be terminated for any cause other than violation of its conditions, the Company will continue to pay to the Manager, his executors, administrators, or assigns, the commissions upon renewal premiums on Intermediate policies as set forth in Section three (3) less a collection fee of two per cent (2%) of such renewal premiums, until the commissions on the premiums in the sixth year of insurance shall have been paid, subject to the conditions of Section twenty-three (23).

Section 7. That if the Manager shall at any time violate any of the conditions of this contract, he shall forfeit all commissions which would thereafter have became payable under this or any previous contract.

Section 8. That if the Manager, at any time after the notice of the termination of this contract, shall take any action toward inducing the agents of the Company to leave its service, or make any attempt to induce its policyholders to relinquish their policies he shall forfeit all commissions which would thereafter have become payable under this or any previous contract.

Section 9. That no commission shall be paid to the Manager on any policy after it has been canceled or become paid-up. But if the Manager, while in the employ of the Company under this contract, shall secure the revival of any policy issued under this contract, after such policy has been canceled, he shall be entitled to the commission on such policy as provided in Sections three (3) and four (4) as though policy had not been canceled.

Section 10. That the Company may make any changes in its methods of conducting its business, may divide the

territory heretofore mentioned and make any other appointments therein.

Section 11. That the Manager shall not insert or authorize the insertion of any advertising matter in any publication whatever, or issue or circulate or authorize the issuing or distribution of any circulars or papers, or write or authorize the writing of any letters to any publication respecting any life insurance company, and that the Manager shall not use or authorize the use of language, orally or in writing, respecting any company tending to bring such company into disrepute.

Section 12. That the Manager shall send to the Company *an exact copy* of all contracts and amendments thereto entered into with agents; that when contracts are terminated, the Manager shall notify the Agent by letter of such termination and shall immediately send to the Company a copy of such letter together with termination form; that such agent shall have no claim against the Company, but in case of the termination of this contract the Company may and is empowered to carry out at its option any agreements as to the payment of renewal commissions contained in the contracts of any agents which may have been terminated by the termination of this contract, and that all payments made to agents by the Company on account thereof shall be deducted from the amounts payable to the Manager, his executors, administrators or assigns, by the terms of this contract; that the Manager shall in no case make a contract with an agent providing for greater compensation than that provided for in this contract; that the Company will not approve any contract between the Manager and an agent in which renewal commissions on Regular policies have been al-

lowed beyond the tenth year of insurance or in which renewal commissions on Intermediate policies have been allowed beyond the sixth year of insurance. And the Manager further agrees to promptly terminate any contract or agreement with an agent when requested by the Company so to do.

Section 13. That the branch office occupied by the Manager shall be subject to the Company's control. If a written lease is required, it must be in the Company's name and a copy filed at the Home Office, and the Manager shall not negotiate a lease unless authorized in writing by the Company so to do. In case there is no written lease, the office is to be wholly under the control of the Company. These conditions apply whether the Manager or the Company pays the rent.

Section 14. That the Manager shall be governed in the business of his Agency by the written and printed instructions and rules which he may from time to time receive from the Company; that he shall keep correct accounts and records of all business done and moneys collected, and that all books, accounts, documents, vouchers and other papers connected with the business of the Company are and shall be its property, and at any time open to the inspection and examination of its authorized representative; and that the Manager shall report to the Company in writing, at such times as he may be instructed so to do the collection of all premiums on policies and receipts sent to him for collection to the date of such accounting.

Section 15. That all moneys or securities received or collected for or on behalf of the Company, after making such deductions as are herein allowed, shall be held by the

Manager as a fiduciary trust, and shall not be used by him for any purpose whatsoever, except as herein specifically authorized, but shall be immediately deposited, in a bank designated by the Company, to the credit of The Prudential Insurance Company of America, or shall be paid over to such person as the Company may designate.

Section 16. That the Manager shall not incur or authorize the incurring of any expense or expenditure whatever on account of this Company without the written authority of the Company.

Section 17. That the Manager has no authority on behalf of the Company to make, alter or discharge any policy, to extend the time for paying a premium, to waive forfeitures, to incur any liability on behalf of the Company, to allow the delivery of any policy unless the applicant be in good health and the first premium paid in full, or to receive any money due or to become due to the Company except on policies and renewal receipts signed by the President, one of the Vice Presidents or the Secretary of the Company and sent to him for collection.

Section 18. That, unless otherwise, terminated, this contract may be terminated by either party by a notice in writing delivered personally, or mailed to the other party at the last known address, at least thirty days before the date therein fixed for such termination. In case the Manager fails to comply with any of the duties, conditions or obligations of this contract, the Company may terminate same upon immediate notice.

Section 19. That when policies issued under this contract are changed and allowance is made on an old policy and applied on a new policy, no commission shall be paid on the amount thus allowed, unless authorized by the

Company; that if the Company shall return premiums on a policy issued under this contract, the Manager shall repay to the Company, on demand, the amount of commissions received on the premiums so returned.

Section 20. That no assignment of commissions earned or accrued or to accrue under this contract shall be valid unless authorized in writing by the Company.

Section 21. That if this contract be terminated, the compensation paid to the Manager, with the amount then due him under this contract, shall be in full settlement of all claims and demands in favor of the Manager under this contract, and that all compensation which a continuance of this contract might have secured to him shall be forfeited, except as herein provided.

Section 22. That the Manager shall not pay or allow, or offer to pay or allow, as an inducement to any person to insure, any rebate of premium or any inducement whatever not specified in the policy.

Section 23. That the Company shall have and is hereby given a first lien upon any commissions or claims for commissions under this or any prior contract, as security for the payment of any claims due or to become due to the Company from said Manager; and the Manager shall pay interest on any outstanding indebtedness at the rate of five per cent (5%) per annum, the interest to be computed at the end of each contract year on the average indebtedness existing during such year.

Section 24. That when a policy issued under this agreement is the cause, directly or indirectly, of the cancelation of a policy previously issued by the Company, the Company reserves the right to adjust the payment of com-

missions as the circumstances of the case seem to warrant.

Section 25. That no compensation shall be allowed on any premium, or portion thereof, payment of which is waived because of the Disability clause contained in the policy.

Section 26. That this contract shall take effect on the Fourth day of August, 1919, when signed by the Manager, and executed on behalf of the Company by the President and one of the Vice-Presidents or by the President and the Secretary.

In Witness Whereof, the parties to this contract have executed the same in duplicate on the day and year first above written.

The Prudential Insurance Company of America
Party of the First Part

By

Forrest F. Dryden, President
Edward Gray, Vice President
Claude R. Fooshe,
Party of the Second Pt

Countersigned by
Hno. H. Rudett
Asst. Secretary

THE PRUDENTIAL INSURANCE COMPANY OF AMERICA

Incorporated under the laws
of the State of New Jersey

Edward D. Duffield, Pres.

Home Office, Newark, New Jersey

IT IS HEREBY AGREED by and between The Prudential Insurance Company of America, and C. R. FOOSHE, Manager for the said Company, that in consideration of the surrender by each of the said parties of their respective rights under all provisions in the existing contract, as heretofore amended, between the said Company and the said Manager concerning the payment of collection fees and the payment of commissions after termination of said contract, as heretofore amended, such provisions are hereby repealed and terminated as of the date of the execution of this agreement, and in place thereof the following provisions are hereby substituted effective from the date hereof.

COLLECTION FEES.

That after commissions, upon policies written by or through said Manager, are no longer payable under the contract, as heretofore amended, of which this is an amendment, and as amended hereby, and hereinafter referred to as this contract, the said Company shall pay to the said Manager a collection fee of two per cent. (2%) of the premiums of all such policies and upon premiums of all policies transferred to him for collection, when in either case such premiums are collected by or through him, excepting that such collection fee on premiums in any policy year on group insurance policies shall be two per cent (2%) of the first $50,000 of the premiums of each

such policy, and one per cent (1%) on the next $150,000 of premiums of each such policy, but no collection fee shall be payable on any part of such premium which is in excess of $200,000; nor, except as hereinafter provided, shall a collection fee be paid to said Manager upon any premiums when collected by or through his agency under this contract concerning which said Company has waived, by agreement, its right to deduct any collection fee from the commissions payable to some other Manager or his estate, where such waiver is in accordance with the agreement of said Company with such other Manager; and only one per cent (1%) collection fee shall be payable to said Manager on any premiums concerning which the Company has agreed to deduct but one per cent (1%) from the commissions payable to some other Manager or his estate.

Terminal Commissions

That if this contract be terminated the compensation to be paid the Manager thereafter shall be:

(a) If terminated by the death of the Manager, his retirement at age 65 or later, his total and permanent disablement, or the withdrawal of the Company from the territory set forth in this contract, the Company will pay the Manager, his executors, administrators or assigns, commissions when and as set forth in this contract, less a collection fee of one per cent (1%); provided, however, that where the Manager is obligated to pay an agent or a broker a renewal commission of five per cent (5%); or a renewal commission of two and one-half per cent (2½%) or more upon premiums on which said Manager is entitled under this contract to but five per cent (5%) renewal commission, no collection fee shall be deducted from the said commissions as set forth in this contract,

during the period for which such renewals are payable to the said agent or broker.

(b) If terminated for any cause other than those mentioned in Paragraph, a or c hereof, the Company will pay to the Manager, his executors, administrators or assigns, commissions, when and as set forth in this contract, up to and including but not beyond the tenth policy year, less a collection fee of two per cent (2%) provided, however, that if the Manager has not been continuously in the service of the Company for at least two years no such commissions will be payable beyond the sixth policy year.

(c) If terminated because he has paid or offered to pay or allow as an inducement to any person to insure any rebate of premium, or if the Manager either during the continuance or after the termination of this contract shall default in the payment to the Company of premiums collected by him or shall take any action towards inducing the Agents of the Company to leave its service or make any attempt to induce its policyholders to relinquish their policies, he shall forfeit all commissions which have otherwise been reserved to him by this or any previous contract.

In Witness Whereof the parties hereto have executed this amendment in duplicate on the 17th day of May, 1927.

The Prudential Insurance Company of America

By

Asst. Secretary

Claude R. Fooshe,

Manager